This record is a partial extract of the original cable. The full text of the original cable is not available.

UNCLAS SECTION 01 OF 03 DUBLIN 001753

SIPDIS

SENSITIVE

E.O. 12958: N/A
TAGS: ECON EFIN SOCI
SUBJECT: IRELAND'S 2005 GOVERNMENT BUDGET

REF: Dublin 1704

¶1. (SBU) Summary: Tax relief and social welfare spending increases are the marquis features of the 2005 Irish Government Budget, a reflection of the Government's newly embraced "caring" image. The Budget provides for a 9 percent increase in government spending over 2004, slightly above the increase projected in the November 18 Budget Estimates. Tax relief will take minimum-wage earners out of the tax net and will widen income tax bands to allow more workers to pay tax at the 20 percent rather than 45 percent rate. Regarding social welfare, the Government will increase pension, unemployment, and child support payments and launch a multi-year funding program for the disabled. Opposition political parties characterized the Budget as a populist attempt to undo the social "damage" done by former Finance Minister Charlie McCreevy. A propitious economic environment will position Cowen in subsequent budgets to strengthen the Government's "caring" image as well as his own credentials to succeed Prime Minister Ahern as party leader over the longer term. End summary.

Overview

¶2. (U) On December 1, Finance Minister Brian Cowen presented to Parliament a Government Budget for 2005 that most prominently featured tax relief and social welfare spending increases. The Budget provides for nearly euro 45 billion in public spending, euro 3.7 billion (9 percent) more than 2004. This increase is above the 6-7 percent spending jump forecast by Cowen in the November 18 Budget Estimates (reftel). Budgetary targets for 2005 include: a government deficit of 0.8 percent of GDP: an exchequer borrowing requirement of just under euro 3 billion, or 2 percent of GDP; and, a debt ratio of 30 percent of GDP. Cowen, who was appointed Minister in September, noted that the 2005 Budget would be his first installment in a three-year effort to strengthen public services (ahead of the 2007 general elections). He also said that budgetary measures on tax relief and social welfare "gave the lie to those who claim that this Government is indifferent to the needs of some of the most vulnerable members of our society" (a response to criticism that the ruling Fianna Fail party's uncaring attitude toward social issues accounted for its poor showing in local and European Parliament elections last June).

Social Welfare

¶3. (U) The first pillar of the 2005 budget is a record euro 12.3 billon package for social welfare. Cowen had announced a euro 300 million increase for social welfare in the November 18 Budget Estimates, and he added another euro 874 million to the final welfare package, for a total increase of euro 1.1 billion, or 8 percent, over ¶2004. Social and Family Affairs Minister Seamus Brennan said that funding increases would benefit 970,000 people, a quarter of the population, who claim regular social welfare payments. Key components of the package are: a euro 12 per week increase in state pensions; a euro 14 per week jump in unemployment and non-pension welfare benefits; and, a monthly euro 10-12 per child increase in child benefits. The 2005 budget also includes increased funding for maternity benefits, non-child-related family income supplements, and respite care grants. The total welfare package reverses roughly half of the social spending cuts introduced in the 2004 Budget.

¶4. (U) A centerpiece of the budget's social agenda is a euro 900 million package for disability services covering 2006-2009 -- the first time that the Government has taken a multi-year approach to the sector. The package comes in addition to a euro 2.8 billon planned expenditure on disability for 2005, an increase of euro 290 million, or 11 percent, over 2004. Total funding over the next four years will: provide more than 4,500 respite centers for the disabled; transfer roughly 600 people with mental disabilities out of psychiatric hospitals; establish 400

community-based mental health facilities; and, provide 1.2 million extra hours of home support and personal assistance. Cowen noted that disability services had previously "been at the end of the queue" for government resources, but would feature prominently in future budget allocations. Disability support groups welcomed the funding increases, but warned that the Disability Bill, published in October, could undermine the budget package in restricting the definition of "disabled" and failing to provide rights to disability services.

Tax Relief

¶5. (U) The second pillar of the 2005 Budget is broad-based tax relief, estimated to cost euro 682 million. The central components of this pillar are:

a) Personal Taxation: The standard rate tax band (with a personal tax rate of 20 percent) was increased by euro 1,400 for a single person to euro 29,400 and by euro 2,800 to euro 58,800 for a dual-income married couple. This widening of the standard rate tax band, the first in three years, means that over 52,000 workers will no longer have to pay tax at the higher 42 percent rate. (Modest wage inflation, however, could push many of these back into the higher tax band in the coming years.) In addition, those earning the minimum wage, euro 7 per hour, will fall outside the tax net.
b) Stamp Duty: The threshold at which stamp duty is charged to first-time buyers of second-hand houses was increased from euro 190,500 to euro 317,500. Second-hand homes sold for between euro 317,501 and euro 381,000 will have stamp duty charged at 3 percent (down from 4.5 percent), and a 6 percent rate will apply to houses sold for between euro 381,001 and euro 635,000 (down from 7.5 percent). (This form of tax relief targets young urban professionals who have had difficulty in recent years affording a first home.)

c) Excise Duty: No changes were made to the main VAT (Value Added Tax) and excise rates in the 2005 Budget. Minister Cowen said he decided against excise duty increases on cigarettes because of hardships that the new smoking ban in enclosed public places had imposed on smokers (cigarettes sales fell by 17.6 percent in the first 10 months of 2004, and tobacco excise collections will be euro 128 million below forecast). Cowen also argued that an increase in duties for cigarettes and alcohol would have created inflationary pressures.

¶6. (U) Responding to public complaints that more than 40 Irish citizens with incomes over euro 500,000 legally avoided taxes in 2004, Minister Cowen announced that he would initiate a comprehensive reform of tax incentive schemes. He has instructed the Department of Finance, in conjunction with the Revenue Commissioners, to evaluate the effect of incentive reliefs and exemptions, with the aim of improving tax system equity.

Capital Expenditures

¶7. (U) The Government will spend euro 36.3 billion on improving the State's infrastructure in the period 2005 - 2009, a proportion of GDP that is nearly twice the EU average. Euro 6.3 billion in Exchequer capital will be made available in 2005, including euro 237 million carried over by Government Departments from 2004. Roughly euro 10.2 billion (28 percent) of the 2005-2009 capital envelope will be invested in transport infrastructure, which the Government regards as key to economic competitiveness and balanced regional development. In his Parliament speech, Cowen stated that he was "extremely conscious of the need to optimize the value for money from the very significant levels of capital funding now in place" (a response to criticism that capital spending in recent years had not yielded appreciable infrastructure upgrades).

Defense, Foreign Affairs, ODA

¶8. (U) The 2005 Budget provides roughly euro 758 million for the Irish Department of Defense, or 1.7 of total government spending. The Department of Foreign Affairs will receive euro 197 million. The Budget will allocate euro 60 million for Official Development Assistance (ODA), a 15 percent increase over 2004. ODA funds will come out of the euro 535 million set aside for International Cooperation, a distinct basket from Foreign Affairs. The Irish Government has also committed to minimum funding of euro 65 million for ODA in both 2006

and 2007. (With a euro 60 million outlay in 2005, ODA will reach 0.4 percent of GNP, in contrast to the Government's Millennium commitment to bring ODA to 0.7 of GNP by 2005. This shortfall has prompted criticism from Ireland's international charitable organizations.)

Reactions

¶9. (U) Opposition political parties characterized the Budget as an attempt to repair the social "damage" done by Former Finance Minister and EU Commissioner-designate Charlie McCreevy. (This view holds that McCreevy emphasized wealth-creation to the neglect of social spending.) Fine Gael spokesperson on Finance, Richard Bruton, described the Budget as "pretending to say sorry" and "designed to bury the McCreevy image." While he conceded that income tax would fall for most people in 2005, he stressed that this would not make up for increases in the cost of living in recent years. Joan Burton, Labour's Finance spokesperson, called the budget a "populist" rather than "visionary" document, "full of half-measures." In a reference to Fianna Fail's 2002 election slogan of "a lot done, a lot more to do," she described the Budget as "some damage undone, a lot more to do". Echoing these sentiments, Dan Boyle, the Green party spokesperson on Finance, said it would take half a dozen such budgets "before you would even begin to repair the damage the last seven budgets have done".

¶10. (U) Prominent businesses and social organizations were generally positive, though cautious, in their reactions to the Budget. Most Irish firms interviewed by the press welcomed the Budget's tax cuts and welfare increases as stimuli for consumer spending, which has flagged in recent years. Indigenous Irish software firms and the U.S. Chamber of Commerce, however, expressed disappointment that the Budget did not target Ireland's competitiveness by providing incentives for scientific research and development. Social organizations generally praised budgetary measures to help the disadvantaged and disabled, though some criticized the Budget as not going far enough. The Children's Rights Alliance said that child benefit increases would not reduce the number of children living in poverty. The National Women's Council and labor unions also faulted the Budget for failing to alleviate high daycare costs for children.

Comment: Santa Cowen

¶11. (SBU) Comment: In the spirit of the season, Irish newspapers have run political cartoons of Cowen dressed as Santa Claus, doling out tax breaks and welfare checks to a disaffected electorate. The cartoons emphasize the point noted in reftel that the 2005 Budget was framed to target popular perceptions of ruling Fianna Fail party's indifference to social concerns. Cowen was fortunate insofar as a euro 2.3 billion overshoot in 2004 tax revenues made possible large giveaways in social welfare spending for 2005, without pushing the projected fiscal deficit close to the EU Growth and Stability Pact ceiling of 3 percent of GDP. Cowen also stands to benefit from Ireland's most propitious macro-economic environment in 4 years, with GDP growth of at least 5 percent predicted through 2006 and an inflation rate that, after many years, has converged toward the 2 percent eurozone average. The Finance Minister is thus positioned to strengthen the Government's "social" credentials further in the two budgets that remain before the 2007 general elections. Those budgets will likely extend benefits beyond the disadvantaged to more of the middle class, with possible child daycare subsidies and additional tax relief for dual-income families. Ireland's positive budgetary and macro-economic outlook will also improve Cowen's own credentials as the reported favorite candidate to succeed Prime Minister Ahern as Fianna Fail leader over the longer term.

KENNY